

**Memorandum**

Date **MAY 28 2002**
Thomas D. Roslewicz
From Thomas D. Roslewicz
Deputy Inspector General
for Audit Services

Subject Review of Additional Benefits Reported by PacifiCare of Texas in the Calendar Year 2000
Adjusted Community Rate Proposal for its San Antonio, Texas Plan (A-06-01-00064)

To Neil Donovan
Director, Audit Liaison Staff
Centers for Medicare & Medicaid Services

As part of self-initiated audits by the Office of Inspector General, we are alerting you to the issuance of the subject audit report within 5 business days from the date of this memorandum. A copy of the report is attached. We suggest you share this report with the Centers for Medicare & Medicaid Services, Health Plan Benefits Group. This report provides the results of our review of additional benefits reported by PacifiCare of Texas (PacifiCare), in the Calendar year (CY) 2000 Adjusted Community Rate Proposal (ACRP) for the San Antonio, Texas plan.

The objectives of our review were to assess whether:

- additional benefits estimated in the ACRP were available to Medicare beneficiaries in accordance with PacifiCare's marketing materials;
- estimated costs in the ACRP for the additional benefits were reasonable when compared to costs actually incurred; and
- additional benefits offered were properly valued, and Medicare beneficiaries enrolled in the plan received value in excess of the co-payments required to obtain the benefits.

Our review showed that the additional benefits estimated in PacifiCare's CY 2000 ACRP were available to Medicare beneficiaries at the levels and co-payments priced in the ACRP, except for additional chiropractic care services. PacifiCare estimated \$107,355 for additional chiropractic services that were not supported or offered to its members.

Our review of other estimates for additional benefits showed they were reasonable compared to the cost actually incurred for CY 2000, except for the cost estimate for hearing services totaling \$455,185. We could not determine the reasonableness of this estimate. PacifiCare could not identify the actual cost associated with additional hearing services, including hearing exams and aids, because it was co-mingled with other costs in PacifiCare's accounting records.

Regarding whether additional benefits were properly valued, we focused our review on the additional drug benefit. Our analysis showed that the additional drug benefit estimated in PacifiCare's CY 2000 ACRP was properly valued, and Medicare members received value in excess of the co-payments required. PacifiCare provided drugs to Medicare members at reduced rates by taking advantage of discounts negotiated with independent pharmacies that dispensed the drugs. Our review of 1998 base year costs reported in the CY 2000 ACRP showed that costs for the additional drug benefit were also reduced by the pharmacy discounts received.

However, PacifiCare could not provide a complete copy of one of the pharmacy contracts we requested for review.

PacifiCare reviewed the draft report and agreed with our audit results and stated that it (1) revised the ACRP preparation and pricing methodology to ensure that only additional benefits available to Medicare beneficiaries are included in the ACRP; (2) examines the accounting system and supporting documentation annually to ensure that appropriate detail data is available for all material Medicare benefits; and (3) monitors the controls for maintaining copies of all provider contracts.

Any questions or comments on any aspect of this memorandum are welcome. Please address them to George M. Reeb, Assistant Inspector General for Health Care Financing Audits, at (410) 786-7104 or Gordon L. Sato, Regional Inspector General for Audit Services, Region VI, (214) 767-9206.

Attachment

Department of Health and Human Services

**OFFICE OF
INSPECTOR GENERAL**

**REVIEW OF ADDITIONAL BENEFITS
REPORTED BY PACIFICARE OF TEXAS
IN THE CALENDAR YEAR 2000
ADJUSTED COMMUNITY RATE
PROPOSAL FOR ITS
SAN ANTONIO, TEXAS PLAN**



**JANET REHNQUIST
Inspector General**

**May 2002
A-06-01-00064**



DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General

Office of Audit Services
1100 Commerce, Room 6B6
Dallas, TX 75242

MAY 31 2002

Common Identification Number: A-06-01-00064

Ms. Tawny Schaffer
PacifiCare of Texas
Suite 600
5001 LBJ Freeway
Dallas, Texas 75244-6130

Dear Ms. Schaffer:

Enclosed are two copies of the U.S. Department of Health and Human Services (HHS), Office of Inspector General (OIG), Office of Audit Services' (OAS) report entitled, "Review of Additional Benefits Reported by PacifiCare of Texas in its Calendar Year 2000 Adjusted Community Rate Proposal for its San Antonio, Texas Plan." A copy of this report will be forwarded to the action official noted below for his review and any action deemed necessary.

Final determination as to actions taken on all matters reported will be made by the HHS action official named below. We request that you respond to the HHS action official within 30 days from the date of this letter. Your response should present any comments or additional information that you believe may have a bearing on the final determination.

In accordance with the principles of the Freedom of Information Act (5 U.S.C. 552, as amended by Public Law 104-231), OIG, OAS reports issued to the Department's grantees and contractors are made available, if requested, to members of the press and general public to the extent information contained therein is not subject to exemptions in the Act which the Department chooses to exercise. (See 45 CFR Part 5). As such within 10 business days after the final report is issued, it will be posted on the world wide web at <http://www.oig.hhs.gov>.

To facilitate identification, please refer to Common Identification Number A-06-01-00064 in all correspondence relating to this report.

Sincerely,

Gordon L. Sato
Regional Inspector General
for Audit Services

Enclosure

Page 2 – Ms. Tawny Schaffer

Direct Reply to HHS Action Official:

Dr. James R. Farris, MD
Regional Administrator
Center for Medicare & Medicaid Services
1301 Young Street, Room 714
Dallas, Texas 75202



Common Identification Number: A-06-01-00064

Ms. Tawny Schaffer
PacifiCare of Texas
Suite 600
5001 LBJ Freeway
Dallas, Texas 75244-6130

Dear Ms. Schaffer:

This report provides the results of our review of additional benefits reported by PacifiCare of Texas (PacifiCare), in the Calendar Year (CY) 2000 Adjusted Community Rate Proposal (ACRP) for the San Antonio, Texas plan. This plan offered managed care services to Medicare members under Medicare+Choice contract number H-4590.

The objectives of our review were to assess whether:

- additional benefits estimated in the ACRP were available to Medicare beneficiaries in accordance with PacifiCare's marketing materials;
- estimated costs in the ACRP for the additional benefits were reasonable when compared to costs actually incurred; and
- additional benefits offered were properly valued, and Medicare beneficiaries enrolled in the plan received value in excess of the co-payments required to obtain the benefits.

Our review showed that the additional benefits estimated in PacifiCare's CY 2000 ACRP were available to Medicare beneficiaries at the levels and co-payments priced in the ACRP, except for additional chiropractic care services. PacifiCare estimated \$107,355 for additional chiropractic services that were not supported or offered to its members.

Our review of other estimates for additional benefits showed they were reasonable compared to the cost actually incurred for CY 2000, except for the cost estimate for hearing services totaling \$455,185. We could not determine the reasonableness of this estimate. PacifiCare could not identify the actual cost associated with additional hearing services, including hearing exams and aids, because it was co-mingled with other costs in PacifiCare's accounting records.

Regarding whether additional benefits were properly valued, we focused our review on the additional drug benefit. Our analysis showed that the additional drug benefit estimated in PacifiCare's CY 2000 ACRP was properly valued, and Medicare members received value in excess of the co-payments required. PacifiCare provided drugs to Medicare members at reduced rates by taking advantage of discounts negotiated with independent pharmacies that dispensed the drugs. Our review of 1998 base year costs reported in the CY 2000 ACRP showed that costs for the additional drug benefit were also reduced by the pharmacy discounts received.

However, PacifiCare could not provide a complete copy of one of the pharmacy contracts we requested for review.

We are recommending that PacifiCare:

- evaluate its cost projection methodology to ensure that only additional benefits available to Medicare members are included in the ACRP;
- maintain an accounting system and supporting documentation for the costs associated with the additional benefits offered to Medicare members for all cost categories included in the ACRP; and
- ensure a copy of all pharmacy contracts is maintained.

PacifiCare reviewed the draft report and agreed with our recommendations and stated that it: (1) revised the ACRP preparation and pricing methodology to ensure that only additional benefits available to Medicare beneficiaries are included in the ACRP; (2) examines the accounting system and supporting documentation annually to ensure that appropriate detail data is available for all material Medicare benefits; and (3) monitors the controls for maintaining copies of all provider contracts. The complete text of PacifiCare's response is presented as **APPENDIX A** to this report.

INTRODUCTION

BACKGROUND

PacifiCare received payments totaling \$183,166,797 for an average of about 74,000 members from the Centers for Medicare & Medicaid Services (CMS) for the San Antonio, Texas plan under Medicare+Choice contract number H-4590 for CY 2000. The Medicare ACRP process is designed for Medicare+Choice organizations (M+COs) to present to CMS their estimates of the funds needed to cover the medical and administrative costs of providing the Medicare package of covered services. The ACRP process also includes

providing estimates of additional benefits (e.g., drugs and eyeglasses) the M+CO plans to offer its Medicare enrollees.

An M+CO must complete a separate ACRP for each coordinated care or private fee-for-service plan offered to Medicare beneficiaries. To compute the adjusted community rate (ACR), the M+CO must calculate an initial rate that represents the average commercial (non-Medicare) premium that the M+CO would charge its general non-Medicare-eligible population for the benefits covered under its plan. The M+CO should also calculate a separate initial rate, using the same approach, for each optional supplemental benefit it offers in conjunction with a plan. This initial rate is then adjusted by various factors described in the regulations, including the relative costs to Medicare beneficiaries, to establish an appropriate payment rate that reflects the characteristics of the Medicare population. The M+CO must submit the ACRP on worksheets CMS provides and must supply additional supporting schedules.

Additional benefits include health care services not covered by traditional Medicare as well as reductions in premiums or cost sharing for Medicare-covered services. Additional benefits are specified by the M+COs and are offered to Medicare beneficiaries at no additional premiums. Those benefits must be at least equal in value to the adjusted excess amount calculated in the ACRP. An excess amount is created when the average payment rate (estimated monthly capitation payment to be received from CMS) exceeds the ACR (as reduced by the actuarial value of co-insurance, co-payments, and deductibles under Parts A and B of Medicare). If there is an adjusted excess amount for the plan it offers, the M+CO must provide additional benefits not covered by Medicare and/or reduce charges otherwise allowed for Medicare-covered services. The M+CO must provide these benefits uniformly to all Medicare beneficiaries enrolled in the plan.

OBJECTIVES, SCOPE, AND METHODOLOGY

The objectives of our review were to assess whether:

- additional benefits estimated in the ACRP were available to Medicare beneficiaries in accordance with PacifiCare's marketing materials;
- estimated costs in the ACRP for the additional benefits were reasonable when compared to costs actually incurred; and
- additional benefits offered were properly valued, and Medicare beneficiaries enrolled in the plan received value in excess of the co-payments required to obtain the benefits.

Prescription drugs comprised about 87 percent of PacifiCare's base year costs for additional benefits; therefore, we focused our in-depth analysis on prescription drugs. To accomplish our objective, we reviewed:

- PacifiCare’s CY 2000 ACRP submission and compared it with PacifiCare’s (1) Beneficiary Information Form (BIF) Data Report (currently referred to as the plan benefit package) that was submitted with the ACRP, and (2) marketing materials to ensure consistency of the dollar limits and co-payments.
- PacifiCare’s CY 2000 “Outpatient Drug Formulary” of generic and brand name medications.
- the CY 2000 actual costs for additional benefits and compared these costs with the estimated amount for these benefits in the ACRP.
- a sample of 50 prescription drug claims judgmentally selected from the June 2000 Medicare claims file provided by PacifiCare. We picked claims from the top generic and brand name drugs published in the 2000 edition of the *Red Book*, a drug pricing publication used by the pharmaceutical industry. We (1) verified the claims were paid in accordance with the terms of pharmacy agreements; (2) confirmed the claims were for Medicare members; (3) traced claims to source documents; (4) verified the correct co-payment was charged; (5) compared prices with the average wholesale prices (AWPs) published in the *Red Book*; (6) compared pricing to 2,723 commercial drug claims identified in the June 2000 commercial claim file for 46 of the 50 drugs sampled; and (7) reviewed annual drug claim histories for the 47 members in our sample of 50 claims to determine if the calculation of the annual brand name drug limit was computed correctly.
- the June 2000 Medicare drug claims file and identified 859 claims for 9 Medicare-covered drugs. We selected a sample of seven claims for three of the nine drugs to verify that the drugs were not applied to the annual brand name limit.
- drug benefit contracts to identify the pricing agreements.
- the contract for the additional vision benefit.
- the contract for discounted hearing aid prices.
- PacifiCare’s 1998 base year financial data, which was used to project the CY 2000 ACRP.

We did not audit PacifiCare’s ACRP or its financial records, nor did we conduct a review of the plan’s internal controls, because these steps were not considered necessary to achieve our objectives. Our review was conducted in accordance with generally accepted government auditing standards. Our fieldwork was performed at PacifiCare in San Antonio, Texas and at the OIG/OAS Austin field office during the period July 2001 through March 2002.

RESULTS OF REVIEW

Our review showed that the additional benefits estimated in PacifiCare's CY 2000 ACRP were:

- available to Medicare beneficiaries at the levels and co-payments priced in the ACRP, except for additional chiropractic care services with an estimated cost of \$107,355.
- reasonably priced compared to the cost actually incurred for CY 2000, except for hearing services with an estimated cost of \$455,185. We could not determine if this estimate was reasonable because PacifiCare could not identify the actual cost associated with the additional hearing services.
- properly valued, and Medicare members received value in excess of the co-payments required.

Regarding whether additional benefits were properly valued, we focused our review on the additional drug benefit. Our examination of 50 drug claims showed that PacifiCare provided drugs to Medicare members at reduced rates by taking advantage of discounts negotiated with independent pharmacies that dispensed the drugs. The drug claims tested were (1) paid in accordance with pharmacy agreements, although PacifiCare could not provide a complete copy of one of the pharmacy contracts we requested for review; (2) for Medicare members enrolled in the plan; (3) supported by source documentation; (4) showing the correct (or lower) co-payment; (5) reasonable; and (6) lower, or not materially higher, than commercial claims for the same drug. The annual drug claim histories for our sample showed that the correct amounts, including the pharmacy discounts, were applied to the members' annual brand name prescription drug limit. These discounts were properly applied to the base year costs as well.

<i>Additional Benefits Estimated in CY 2000 ACRP and Available to Medicare Members</i>	PacifiCare's additional benefits submitted with its CY 2000 ACRP included outpatient prescription drugs, vision, dental, hearing, chiropractic, and preventive services. PacifiCare's BIF Data Report and marketing materials showed additional benefits at the levels and co-payments priced in the ACRP, except for the chiropractic care additional benefit. PacifiCare estimated \$107,355 for additional chiropractic services that were not offered to its members. No additional chiropractic services were listed in the BIF Data Report or PacifiCare's marketing materials. PacifiCare's marketing materials only offered limited chiropractic care coverage in accordance with Medicare guidelines, and stated that routine chiropractic services were not covered.
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Because prescription drugs comprised about 87 percent of base year costs for additional benefits, we focused our in-depth analysis on prescription drugs. The drug co-payment amounts listed in the BIF agreed with PacifiCare’s marketing materials. PacifiCare’s prescription drug benefit included an annual limit per enrollee of \$1,500 for brand name drugs and no limit on the amount for generic drugs. Listed below is a schedule of the co-payments required:

Type of Drug	Retail Pharmacy (30-day supply)	Mail Order Pharmacy (90-day supply)
Brand Name	\$15	\$45
Generic	\$5	\$15

We reviewed PacifiCare’s CY 2000 ‘Outpatient Drug Formulary’ that lists the generic and brand name medications available through PacifiCare’s prescription drug benefit plan. It included a number of brand name and generic drugs that were covered and it provided alternatives for excluded drugs. The January 2000 formulary listed 270 brand name drugs, along with their generic equivalents, and an additional 301 generic drugs. The formulary also listed 561 drugs that were not covered. Members can obtain non-covered drugs with a physician’s approval.

<i>Estimated Versus Actual Costs for Additional Benefits</i>	The estimated additional benefit cost of \$107,355 for chiropractic care was not reasonable because PacifiCare did not cover additional chiropractic services beyond what was covered by Medicare. PacifiCare offered limited chiropractic services that were in accordance with Medicare guidelines.
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We could not determine whether estimated additional benefit costs of \$455,185 for hearing services were reasonable compared to actual CY 2000 costs. PacifiCare estimated \$433,714 for hearing exams and \$21,471 for hearing aids. However, PacifiCare’s accounting system did not track additional benefit costs for the hearing services separately. PacifiCare included the cost for additional hearing services under the health care professional cost category. This cost category did not separate the cost for hearing services, or whether the cost was for Medicare-covered services or additional benefits.

Estimated additional benefit costs for the prescription drug benefit were reasonable compared to actual prescription drug costs for CY 2000. Our review showed that PacifiCare expended \$4.98 per member per month (PMPM) more than the estimated drug cost reported in the CY 2000 ACRP.

Estimated additional benefit costs for vision services were reasonable compared to actual costs for CY 2000. Our review showed that PacifiCare overestimated the vision costs by \$.11 PMPM. PacifiCare did not provide the actual vision co-payment amount. Therefore, we used the estimated co-payment in the CY 2000 ACRP in calculating the actual costs.

Additional Benefits Value

Our review of whether the additional benefits were properly valued focused on the additional drug benefit.

Our analysis showed that the drug benefit was properly valued and that Medicare members received value in excess of the co-payments required. The results of our review of PacifiCare's drug pricing terms and the 50 drug claims we examined are detailed below.

PacifiCare's Drug Pricing Terms

PacifiCare contracted with PacifiCare Pharmacy Centers, Inc. (PPC) to administer PacifiCare's pharmacy benefit program. The PPC is a corporation doing business as Prescription Solutions. According to the contract, the relationship between the parties is one of independent parties. The contract required PPC to establish and maintain a network of pharmacies to service the pharmacy benefit program. It also required PPC to enter into rebate agreements on behalf of PacifiCare with drug manufacturers, which have products on the drug formulary. The PPC was required to collect all rebates and disburse them to PacifiCare. The PPC was also responsible for handling drug mail orders directly for both Medicare and commercial members. The rate paid for the mail order brand and generic drugs was AWP less 20 percent, plus a dispensing fee.

The PPC contracted with pharmacies to handle the non-mail orders. The PPC contracted with 16 chain pharmacies, 8 Pharmacy Services Administration Organizations, and 2 independent pharmacies for the San Antonio plan. The following pricing terms were in effect for CY 2000:

Brand Name Drug	Generic Drug
<p><u>Lesser of:</u></p> <ul style="list-style-type: none">• Pharmacy's "usual and customary" price, or• AWP less 15 percent plus a dispensing fee of \$2.00	<p><u>Lesser of:</u></p> <ul style="list-style-type: none">• Pharmacy's "usual and customary" price,• AWP less 15 percent plus a dispensing fee of \$2.00, or• Maximum Allowable Cost plus a dispensing fee of \$2.00

Of the seven pharmacy contracts requested for review, PacifiCare could not provide the complete contract for one pharmacy. PacifiCare only provided the amended Exhibit D that contained the pricing terms. Prescription Solutions and the pharmacy itself were unable to locate the pharmacy agreement.

Sample Review Results

Our review of 50 drug claims showed that PacifiCare paid drug prices in accordance with the contracted pricing agreements and were made for Medicare members enrolled in the plan. The claims were supported by source documentation that confirmed the correct (or lower) co-payment was charged to the member. In addition, the prices paid were reasonable in comparison to the AWP for the same drugs listed in the 2000 edition of the *Red Book*, taking into consideration the discounts listed in the pharmacy contracts. Our review of commercial claims for the drugs in our claim sample did not disclose any instances in which commercial claims were materially lower than Medicare claims for the same drug.

The annual drug claim histories for the members in our sample showed that the correct amounts, including the pharmacy discounts, were applied to the members' annual brand name prescription drug limit. In addition, our testing did not disclose any instance in which Medicare-covered drugs were charged against the annual limit.

CONCLUSION AND RECOMMENDATIONS

Our review showed that the additional benefits estimated in PacifiCare's CY 2000 ACRP were available to Medicare beneficiaries at the levels and co-payments priced in the ACRP, except for additional chiropractic care services. PacifiCare estimated \$107,355 for additional chiropractic services that were not supported or offered to its members. This estimated cost should have been excluded from the ACRP.

Our review of other estimates for additional benefits showed they were reasonable compared to the cost actually incurred for CY 2000, except for the cost estimate for hearing services totaling \$455,185. We could not determine the reasonableness of this estimate. PacifiCare could not identify the actual cost associated with additional hearing services, including hearing exams and aids, because it was co-mingled with other costs in PacifiCare's accounting records.

Regarding whether additional benefits were properly valued, we focused our review on the additional drug benefit. Our review showed that the additional drug benefit estimated in PacifiCare's CY 2000 ACRP was properly valued, and Medicare members received value in excess of the co-payments required. PacifiCare provided drugs to Medicare members at reduced rates by taking advantage of discounts negotiated with independent pharmacies that dispensed the drugs. These reduced rates were properly applied to the base year costs as well. However, PacifiCare could not provide a complete copy of one of the pharmacy contracts we requested for review.

We recommend that PacifiCare:

- evaluate its cost projection methodology to ensure that only additional benefits available to Medicare members are included in the ACRP;
- maintain an accounting system and supporting documentation for the costs associated with the additional benefits offered to Medicare members for all cost categories included in the ACRP; and
- ensure a copy of all pharmacy contracts is maintained.

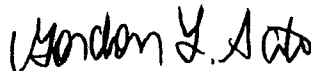
AUDITEE'S COMMENTS

PacifiCare reviewed the draft report and agreed with our recommendations and stated that:

- the additional chiropractic services with an estimated cost of \$107,355 were mistakenly included in the CY 2000 ACRP that were not offered to members. The ACRP preparation and pricing methodology was revised to ensure that only additional benefits available to Medicare beneficiaries are included in the ACRP;
- its accounting system and supporting documentation are examined annually to determine that appropriate detail data is available for all material Medicare benefits. The hearing aid benefit cost included in the ACRP was based on actuarial estimates due to the difficulties in identifying costs for benefits, such as hearing aid coverage, that are provided through capitated contracts. PacifiCare discontinued the hearing aid benefit in subsequent years; therefore, this finding is not a current issue; and
- its policy is to maintain copies of all provider and vendor contracts. However, even with internal controls developed by management, it may not always be possible to locate a specific contract in a limited timeframe. PacifiCare will continue to monitor the controls surrounding this process.

The complete text of PacifiCare's response is presented as **APPENDIX A** to this report.

Sincerely,



Gordon L. Sato
Regional Inspector General
for Audit Services

APPENDIX



5001 LBJ Freeway, Suite 600
Dallas, TX 75244-6130

Common Identification Number: A-06-01-00064

March 14, 2002

Mr. Gordon L. Sato
Regional Inspector General for Audit Services
Office of Inspector General
1100 Commerce, Room 6B6
Dallas, TX 75242-1027

Dear Mr. Sato:

Thank you for the opportunity to respond to the draft report prepared by your office entitled "Review of Additional Benefits Reported by PacifiCare of Texas in its Calendar Year 2000 Adjusted Community Rate Proposal for its San Antonio, Texas Plan." We anticipate that our response will be included in the final report that is issued to CMS.

First, we are pleased that the OIG's review acknowledged that the ACRP was prepared in substantial compliance with current governing standards and regulations.

Summary of Major Findings:

Specifically, the OIG's draft report identifies three primary findings with respect to additional benefits estimated in PacifiCare's CY 2000 ACRP:

1. Additional benefits were available to Medicare beneficiaries at the levels and co-payments priced in the ACRP, except for additional chiropractic care services with an estimated cost of \$107,355. PacifiCare estimated \$107,355 for additional chiropractic services that were not supported or offered to its members.

M+CO Response: We agree that additional chiropractic services with an estimated cost of \$107,355 were mistakenly included in the CY 2000 ACRP that were not offered to members. The ACRP preparation and pricing methodology has been revised to ensure that only additional benefits available to Medicare beneficiaries are included in the ACRP.

2. Additional benefits were reasonably priced compared to the cost actually incurred for CY 2000, except for hearing services with an estimated cost of \$455,185. We could not determine if this estimate was reasonable. PacifiCare could not identify the actual cost associated with the additional hearing services because it is co-mingled with other costs in PacifiCare's accounting records.

M+CO Response: Our accounting system and supporting documentation are examined annually to determine that appropriate detail data is available for all material Medicare benefits.

The hearing aid benefit cost included in the ACRP was based on actuarial estimates due to the difficulties in identifying costs for benefits, such as hearing aid coverage, that are provided through capitated contracts that span multiple benefit categories. The use of actuarial estimates, as well as the consolidation of cost categories, was addressed in our waiver request letter, dated June 7, 1999, to Mr. Frank Regulski, in our follow-up letter to Mr. Mike Shanks, and in our ACRP cover letter, dated July 1, 1999. PacifiCare of Texas discontinued the hearing aid benefit in subsequent years; therefore, this finding is not a current issue.

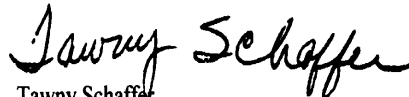
3. The additional drug benefit estimated in the CY 2000 ACRP properly valued, and Medicare members received value in excess of the co-payments required. However, PacifiCare could not provide a complete copy of one of the pharmacy contracts we requested for review.

M+CO Response: Our policy is to maintain copies of all provider and vendor contracts. However, even with the internal controls developed by management, it may not always be possible to locate a specific contract in a limited timeframe. We will continue to monitor the controls surrounding this process.

Conclusion

We appreciate the opportunity to work with your office on this draft report.

Respectfully,

A handwritten signature in black ink that reads "Tawny Schaffer". The signature is written in a cursive, flowing style.

Tawny Schaffer
Director, Finance